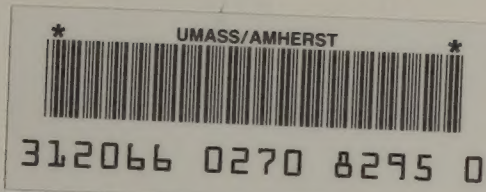


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Commonwealth of Massachusetts
Executive Office of Environmental Affairs

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POLICY AND GUIDELINES

FOR SECURED LENDER LIABILITY UNDER CHAPTER 21E

Policy #WSC-94-602

This policy provides guidance to Department of Environmental Protection (DEP) personnel as to how DEP intends to exercise its enforcement discretion with respect to lenders and creditors who may be potentially liable as an owner/operator under M.G.L. c. 21E.

6/13/94
Date

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943/224

I. Purpose of Policy and Guidance Document

The primary purpose of this policy and guidance document is to provide guidance to DEP personnel as to how DEP intends to exercise its enforcement discretion with respect to lenders and creditors who may be potentially liable as an owner/operator under M.G.L. c. 21E, §§ 5(a) or (b). An additional purpose of this document is to provide such lenders/creditors, as well as other private parties, with information about how DEP generally will handle secured lenders in the enforcement context for purposes of managing their internal affairs. The procedures set out in this document are intended solely for the guidance of DEP personnel. This document is not intended and cannot be relied upon to create rights, substantive or procedural, enforceable by any party in litigation with the Commonwealth.

II. Applicability

This policy and guidance document concerns those lenders and creditors who may be potentially liable as owners/operators under M.G.L. c. 21E, §§ 5(a) or (b). It is intended only to clarify the circumstances in which DEP generally (1) will direct a lender/creditor to undertake a cleanup through the issuance of an Order or Notice of Responsibility; and (2) will seek recovery from a lender/creditor of those response costs incurred by DEP at a 21E site.

Nothing in this document is intended (1) to address those actions DEP otherwise may take against a lender/creditor for any violation of Chapter 21E, the Massachusetts Contingency Plan or other applicable laws; or (2) to affect any party's potential legal liability, or claim to any defense to liability, under Chapter 21E.

III. Why Lender Liability is An Issue

In July, 1992, a series of amendments intended to clarify the extent of a secured lender's liability under Chapter 21E were signed into law. Prior to the 1992 amendments, the 21E definition of "owner/operator" excluded anyone "who, without participation in the management of a site or vessel holds indicia of ownership primarily to protect his security interest in said vessel or site." This provision, known as the "security interest exemption," lacked any criteria as to the types of activities which would constitute "participation in the management" and thereby void the exemption. Furthermore, the term "indicia of ownership," and the requirement that the ownership indicia be held "primarily to protect [the] security interest in the site or vessel," were not otherwise defined.

The applicability of the pre-1992 security interest exemption to a lender/creditor who acquired ownership or possession of a 21E site through such means as foreclosure or acceptance of a deed in lieu of foreclosure has also been the subject of much policy and legal debate. DEP has taken the position in cases in the past, supported in part by caselaw under an analogous provision in CERCLA¹, that this exemption is void upon a lender/creditor acquiring ownership or possession of the subject property.² The result of this DEP practice reportedly has been that many lenders/creditors have opted to forebear exercising their right to acquire ownership or take possession out of fear of incurring potential Chapter 21E liability which would necessarily follow.

The 1992 amendments to Chapter 21E sought to provide additional protection from liability to secured lenders.³ This was accomplished by replacing the pre-1992 security interest exemption in the definition of "owner/operator" with a secured lender exemption. Under this provision, a secured lender is exempted from liability as an "owner/operator" if:

- (1) no act of the secured lender, or the secured lender's employee or agent, causes or contributes to the release or threat of release or causes the release or threat of release to become worse than it otherwise would have been;
- (2) before acquiring ownership or possession of the site or vessel, the secured lender does not participate in the management of the site or vessel;
- (3) after acquiring ownership or possession of the site or vessel, and upon obtaining knowledge of a release or threat of release of oil or hazardous material, the secured lender:

¹ DEP acknowledges the conflicting caselaw which has developed regarding CERCLA's security interest exemption, most notably the *Fleet Factors* and *In re Bergsoe Metals* cases, and notes the absence of any pertinent caselaw under Chapter 21E's security interest exemption.

² While this shield from liability was deemed by DEP to last only until a lender/creditor forecloses on a 21E site, as the landowner, the lender/creditor would have the opportunity to assert an affirmative defense under Chapter 21E.

³ For purposes of this policy, DEP assumes that any lender or creditor entitled to claim the pre-1992 security interest exemption also falls within the reach of the definition of "secured lender" in Chapter 21E, as amended.

(A) notifies DEP immediately upon obtaining knowledge of a release or threat of release in accordance with DEP's regulations;

(B) provides reasonable access to the site or vessel to DEP and to other persons intending to conduct response actions;

(C) undertakes reasonable steps to prevent the exposure of persons to oil or hazardous materials and to contain the further release or threat of release of oil or hazardous materials from a structure or container;

(D) conducts any voluntary response actions at the site or vessel in compliance with Chapter 21E and the MCP; and

(E) acts diligently to sell or otherwise divest itself of ownership or possession of the site or vessel and divests itself of ownership or possession within five years after the secured lender first acquired ownership or possession.

For purposes of the post-1992 secured lender exemption, "participation in the management of the site or vessel" is defined generally to include activities which substantially divest from the borrower or any other person possession or control over those aspects of the operations involving the management of oil or hazardous materials. Moreover, the new provisions make clear that the following activities do not constitute sufficient participation in the management so as to void the exemption:

(A) requiring or conducting assessments of the site or vessel;

(B) engaging in the regular or periodic monitoring of the business conducted at or on the site or vessel;

(C) making the provision of financing conditional on covenants, representations or warranties concerning the proper handling, use, storage, transport or disposal of oil or hazardous materials at or from the site or vessel, the timely and proper response to releases or threats of release of oil or hazardous materials at or from the site, the maintenance of the site or vessel in compliance with Chapter 21E and other applicable laws, or the periodic submission of information concerning oil or hazardous materials at or from the site or vessel;

(D) providing periodic advice, information, guidance or direction concerning the general business and financial aspects of the borrower's operations, excluding advice, guidance or direction concerning the management of oil or hazardous materials;

(E) providing general information regarding a borrower's obligations pursuant to Chapter 21E and the MCP and information of how the borrower may identify and select a licensed site professional and general information regarding a borrower's obligations for the transportation, storage, treatment and disposal of hazardous waste or hazardous materials under applicable laws; and

(F) engaging in financial workouts, restructuring or refinancing of the borrower's obligations, or undertaking activities to protect or preserve the value of the security interest in a site or vessel, excluding activities involving those aspects of the borrower's operations involving the management of oil or hazardous materials.

For purposes of the post-1992 secured lender exemption, "indicia of ownership primarily to protect a security interest" is defined to include only those interests in real or personal property typically acquired and held as security or collateral for payment or performance of an obligation. The amendments define such interests to include a mortgage, deed of trust, lien, security interest, assignment, pledge, or other encumbrance against real or personal property, including those interests which have a contingent interest component, which are furnished by the owner thereof to assure repayment of a financial obligation, and certain contractual participation rights in such interests. The amendments specifically exclude from protection those interests acquired and held to protect any interest in property owned or held for investment purposes, a lease or a consignment which may not be considered a secured transaction under applicable principles of commercial law, interests of a person acting as a trustee of property or of a business, and any interest other than one created as a bona fide security interest in real or personal property.

The 1992 amendments to Chapter 21E, however, included no express provision for the retroactive application of the post-1992 secured lender exemption. The absence of any such provision has created uncertainty, both within and outside of DEP, as to how the pre-1992 security interest exemption and the post-1992 secured lender exemption apply. This policy and guidance document is designed not only (i) to reaffirm DEP's

commitment to the premises underlying the lender liability protection in the amended Chapter 21E, and (ii) to reduce the uncertainty which has resulted as a result of the recent amendments, but also (i) to reward those lenders/creditors who took appropriate risk reduction measures at those 21E sites at which they acquired ownership or possession thereby encouraging such behavior from parties in the future, and (ii) to encourage lenders/creditors either to undertake voluntary cleanup measures or to finance other parties intending to do so.

IV. Statement of Policy

The Department's goal is to treat lenders/creditors subject to the protection of the pre-1992 security interest exemption similarly to the way it treats lenders/creditors subject to the post-1992 secured lender exemption. Accordingly, in applying the pre-1992 security interest exemption to a lender/creditor who is potentially liable under Chapter 21E as an owner/operator, the Department will take into consideration the changes and clarifications to the liability protection afforded secured lenders under the 1992 amendments to Chapter 21E and extend to those lenders/creditors a similar level of protection.

V. Guidance for Application of Policy for Secured Lenders

DEP personnel should consider this guidance in those instances in which (1) the lender/creditor obtained ownership or possession of the subject property prior to July 1, 1992, and divested itself of all ownership and possession prior to July 1, 1992; (2) the lender/creditor obtained ownership or possession of the subject property prior to July 1, 1992, and either divested or intends to divest itself of all ownership and possession after July 1, 1992, and (3) the lender/creditor obtained or obtains ownership or possession of the subject property after July 1, 1992.

(1) Treatment of the holder of a security interest who obtained ownership or possession prior to July 1, 1992, and divested itself of all ownership and possession prior to July 1, 1992.

Any lender/creditor so situated is subject to the pre-1992 security interest exemption in Chapter 21E only. In light of the 1992 amendments to Chapter 21E, DEP will no longer consider a lender/creditor who merely acquired ownership or possession of a 21E site to have lost the

protection of the pre-1992 security interest exemption.⁴ In determining whether a person so situated is entitled to the liability protection of the pre-1992 security interest exemption, DEP personnel should consider whether the lender/creditor (1) participated in the management of the site or vessel, and (2) held indicia of ownership primarily to protect his security interest in the vessel or site.

In determining whether a lender/creditor so situated participated in the management of the site or vessel or held indicia of ownership primarily to protect its security interest therein, DEP should apply the definitions of "participation in the management of the site or vessel" and "indicia of ownership primarily to protect a security interest" found in the post-1992 secured lender exemption.

Accordingly, if the lender/creditor refrained from participating in the management of the site or vessel, held indicia of ownership primarily to protect his security interest in the vessel or site, and is otherwise not liable for the release or threat of release, DEP personnel should take no further enforcement action against the lender/creditor under Chapter 21E to direct it either to undertake the cleanup or to reimburse DEP for DEP's response costs.

(2) Treatment of a holder of a security interest who obtained ownership or possession prior to July 1, 1992, and either has divested or intends to divest itself of all ownership and possession after July 1, 1992.

Any lender/creditor so situated is subject (1) to the pre-1992 security interest exemption with respect to its liability before July 1, 1992, and (2) to the post-1992 secured lender exemption with respect to its liability after July 1, 1992.

In enforcing Chapter 21E, DEP personnel should first analyze whether a lender/creditor so situated was entitled to the liability protection of the pre-1992 security interest exemption considering the criteria set forth in Subsection V(1) above. If DEP personnel believe the lender/creditor is entitled to the pre-1992 security interest exemption, they should next determine, in accordance with this policy and guidance document, whether the lender/creditor has maintained

⁴ DEP notes that its former position may be inconsistent with a developing line of cases under CERCLA's identical security interest exemption. See, e.g., United States v. McLamb, 5 F.3d 69 (4th Cir. 1993), Ashland Oil, Inc. v. Sonford Products Corp., 810 F. Supp. 1057 (D.Minn. 1993), and Waterville Industries v. Finance Authority of Maine, 984 F.2d 549 (1st Cir. 1993).

its liability protection by satisfying the provisions of the post-1992 secured lender exemption.

If DEP personnel do not believe the lender/creditor is entitled to the pre-1992 security interest exemption, they should deem the lender/creditor to have also lost the liability protection afforded by the post-1992 secured lender exemption.

Solely for purposes of determining whether a lender/creditor so situated is protected under the post-1992 secured lender exemption, DEP personnel should consider the lender/creditor to have met the requirements (1) for notifying DEP immediately upon obtaining knowledge of a release or threat of release, and (2) for containing further releases or threats of release from a structure or container, if the lender/creditor either achieved compliance therewith or divested itself of all ownership and possession by July 20, 1993.⁵

In the event that the lender/creditor failed either to provide such notice or divest itself of all ownership and possession by July 20, 1993, and otherwise would not be liable for the release or threat of release, DEP personnel should consider the surrounding circumstances in deciding whether to deem the lender/creditor to have lost the benefit of the new exemption, including whether the release or threat had been previously reported to DEP by another party; those actions, if any, the lender/creditor undertook in response to the release or threat of release; the actual and potential harm that might

⁵ While the Chapter 21E, as amended, is clear in requiring lenders/creditors so situated to provide such notice to DEP *immediately* upon gaining knowledge of a reportable release or threat of release to obtain the benefits of the post-1992 secured lender exemption, it is unrealistic to expect such lenders/creditors to provide this notice to DEP on July 1, 1992, the effective date of the new provisions, especially since the new provisions were not signed into law by Governor Weld until July 20, 1992. By giving these lenders/creditors until July 20, 1993, to provide the required notification to maintain this exemption, DEP is providing a reasonable period of time for lenders/creditors to have learned about the new law and to have taken necessary actions to come into compliance with the new notification requirements in the Massachusetts Contingency Plan.

DEP is considering in another context whether persons subject to Chapter 21E's release notification requirements, including lenders/creditors, must notify DEP upon gaining knowledge of a release or threat of release of oil or hazardous material for which notice was previously provided to DEP by another party.

have resulted from the failure to notify or to take appropriate action; and any other relevant factors--which reasonably might be considered in the exercise of DEP's enforcement discretion.

Solely for purposes of determining under the post-1992 secured lender exemption whether (1) a lender/creditor so situated has divested itself of ownership or possession of the site or vessel within five years, or (2) a lender/creditor so situated is entitled to the eighteen month rebuttable presumption that it is acting diligently to divest itself of ownership or possession, DEP personnel should consider July 1, 1992, the date on which the lender/creditor acquired ownership or possession.

(3) Treatment of a secured lender who obtains ownership or possession after July 1, 1992.

Any lender/creditor so situated is subject to the post-1992 secured lender exemption. DEP personnel should consider on a case-by-case basis whether such a lender/creditor has maintained the liability protection afforded by this exemption before taking further enforcement action against the lender/creditor under Chapter 21E to direct it either to undertake the cleanup or to reimburse DEP for DEP's response costs.

Solely for purposes of determining whether a lender/creditor so situated is protected under the post-1992 secured lender exemption, DEP personnel should consider the lender/creditor to have met the requirements (1) for notifying DEP immediately upon obtaining knowledge of a release or threat of release, and (2) for containing further releases or threats of release from a structure or container, if the lender/creditor either achieved compliance therewith or divested itself of all ownership and possession by July 20, 1993.

VI. Lenders/Creditors who have not Divested all Ownership and Possession

Notwithstanding any provision of this policy and guidance document to the contrary, if DEP incurs response action costs at a 21E site where a lender/creditor entitled to liability protection under Chapter 21E has title to or possession of a 21E site, DEP may seek to perfect a lien on such site in accordance with Chapter 21E and the MCP. Prior to undertaking any response actions, DEP personnel should attempt to notify the lender/creditor of its intent to take such actions in accordance with Chapter 21E and provide the lender/creditor with a reasonable opportunity to take such actions, even though the lender/creditor has no legal responsibility to do so.

VII. Issuance of Requests for Information and Notices of Responsibility

Prior to issuing Notices of Responsibility to a lender/creditor who has acquired ownership or possession of a 21E site, DEP personnel should make reasonable efforts to gather appropriate information, through such methods as the issuance of Requests for Information (RFI) and other investigative techniques, to determine whether the lender/creditor who acquired ownership or possession of a 21E site satisfies the criteria set forth above and in Chapter 21E for liability protection. DEP expects lenders/creditors to cooperate by responding fully and timely to reasonable requests for information.

VIII. Treatment of Lender's and Creditor's Corporate Officers, Directors and Shareholders

DEP generally follows traditional doctrines of corporation law in enforcing Chapter 21E, including the generally accepted rule that corporate officers, directors and shareholders are not individually responsible for the liabilities of a corporation. Nevertheless, there are exceptions⁶ to these traditional corporate doctrines that allow a court to hold individual officers, directors and shareholders in controlling positions liable for the environmental liabilities of a corporation. Because the caselaw in this area is somewhat unsettled and evolving, DEP personnel should consult with counsel prior to issuing an order or Notice of Responsibility to an individual officer, director or shareholder of a corporation.

IX. Effective Date

This policy and guidance document is effective immediately and must be fully followed by all DEP personnel in enforcing Chapter 21E. Any exceptions to the guidance set forth above must be approved by the Assistant Commissioner for the Bureau of Waste Site Cleanup.

⁶ For instance, individual officers, directors and shareholders having authority to control the disposal of hazardous waste, or a high degree of involvement in the operations of a polluting facility, have been held personally liable for corporate environmental liabilities.

